



U.S. DEPARTMENT OF COMMERCE
BUREAU OF INTERNATIONAL COMMERCE
WASHINGTON, D.C. 20230

March 3, 1967

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MEMORANDUM

TO: Messrs. Nathaniel Davis (White House)
Winn Finner (Agriculture)
Robert Wright (State)
Joseph P. Goldberg (Labor)
✓ William N. Morell (CIA)
Martin I. Goodman (Maritime Administration)
Sherman Abrahamson (Commerce/OEC); and
Richard E. Hull (Commerce/GCO)

FROM: Theodore L. Thau
Executive Secretary
Advisory Committee on Export Policy

SUBJECT: Study on Wheat and Feed Grains

Attached is a redraft of our summary report, with conclusions and recommendations, dated March 1, 1967. It corrects some errors found in the previous draft and makes a few editorial improvements.

As you have told me that the February 14 version, with its errors corrected, would be acceptable to you as a draft suitable for submission to our respective department and agency heads, I have sent a copy of this March 1 redraft to Secretary Trowbridge, and recommend that you now follow a like course. Please advise your department or agency heads that, because the conclusions and recommendations in this draft relate to, but do not take into account, the new national maritime policies and programs which are only now being developed by Secretary Boyd of the Department of Transportation, Secretary Trowbridge is sending him a copy of this draft.

Secretary Trowbridge plans to get in touch soon with your department and agency heads, as well as with Secretary Boyd. Meantime, he welcomes any comments and suggestions they may wish to advance.

Attachment

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SUMMARY, CONCLUSIONS, AND RECOMMENDATIONS

As a major world wheat exporter and the principal supplier of feed grains to world markets, the U.S. is capable of competing for such markets throughout the world, including the East European Communist countries and the USSR. Because of increased costs and other burdens resulting from shipping (and related export licensing) restraints imposed by the U.S. Government, U.S. firms are unable to share in the wheat and feed grain purchases of certain of these countries to the extent they might if these restraints were removed.*

The shipping restraints in question are, in substance, that 50% of wheat and feed grain cargoes to the USSR must be carried in U.S.-flag ships; that 50% of wheat cargoes to Albania, Czechoslovakia, Hungary, Bulgaria and East Germany must also be carried in U.S.-flag ships. With respect to feed grain cargoes to the last five named countries, this 50-50 rule also applies, but it is waived, and the entire cargoes are permitted to be carried in foreign flag ships, if part of each such cargo is destined for and first unloaded in a West European or Mediterranean country, including Yugoslavia. This 50%, or 50-50, rule or restraint will be referred to as such hereafter. The part-cargo unloading procedure, though sometimes called the part-cargo rule or restraint, is more properly considered a "relaxation" or "waiver" of the 50-50 rule, which would otherwise apply to feed grain shipments to Albania, Czechoslovakia, Hungary, Bulgaria and East Germany. (The significance of this distinction is that termination of the so-called "part-cargo rule" alone would only reinstate the more stringent 50% U.S.-flag ship rule for such shipments.)

* This study is not concerned with the question of removing U.S. foreign policy restraints on grain sales which are part of our embargo of substantially all trade with Communist China, North Vietnam, North Korea and Cuba.

CONFIDENTIAL

-2-

The U.S. export licensing restraints referred to above are to enable the Commerce Department to make sure that the conditions of the 50% shipping restraint and the part-cargo relaxation are met by U.S. exporters of wheat and feed grains to the affected countries.

In accord with special foreign policy considerations relating to U.S. exports to Yugoslavia, Poland and Romania, the aforementioned shipping and export licensing restraints are not applied to our wheat and feed grain exports to those East European countries. Shipments to them may go freely in foreign-flag vessels, subject to only one qualification which is applicable to Poland and Rumania. Although a "part cargo" of feed grains may be first unloaded in and destined for Yugoslavia, with the balance destined for Albania, Czechoslovakia, Hungary, Bulgaria or East Germany, the U.S. does not also permit Poland or Romania to be the recipient of the "part cargo".

The purpose of this study is to aid government policymakers in deciding whether economic and foreign policy benefits that might flow from removal of the U.S. restraints on sales of wheat and feed grains to the USSR, as well as to Albania, Bulgaria, Czechoslovakia, East Germany and Hungary (hereafter called "the restricted countries of Eastern Europe"), would outweigh the domestic risks and costs that might arise from that action.

The attachments are the several parts of this study made by Agriculture, CIA, Commerce, Labor, Maritime Administration, and State officials, relative to various aspects of the question of removing U.S. restraints on sales of wheat and feed grains to the restricted countries of Eastern Europe and the

CONFIDENTIAL

CONFIDENTIAL

-3-

USSR. They deal with (a) the grain production, consumption and import requirements of the several countries; (b) the extent to which the expected import requirements of the USSR and the restricted countries of Eastern Europe might result in increased opportunities for such sales by U.S. firms; and (c) the merits and mechanics of repealing or modifying the present U.S. restraints--the 50-50 shipping requirement and its part-cargo unloading exception--to make the U.S. more competitive in the USSR and the restricted countries of Eastern Europe. This paper represents the agreed assessment of these officials of the several departments and agencies who took part in preparing the study, except that the CIA representatives' role was confined to an assessment of the grain positions of the various countries.

The Communist Markets

The Communist countries of the world, as a whole, are a growing but uncertain market for free world grains, mainly wheat. In the present crop Year* they will probably buy 12 - 14 million tons of free world wheat. Of this, 5 - 7 million tons will probably be Communist Chinese purchases. The balance will be taken mainly by the USSR and to a lesser extent by the restricted countries of Czechoslovakia, East Germany, Bulgaria and Hungary,

* Year ending June 30, 1967.

CONFIDENTIAL

CONFIDENTIAL

-4-

and the non-restricted countries of Poland and Yugoslavia.* In addition, the Communist countries will likely take upward of 1 - 1.5 million tons of free world feed grains this year--almost wholly in the restricted countries of Czechoslovakia, East Germany, Hungary, and Bulgaria, and also in Poland.

It is considered likely that both the USSR and the restricted countries of Eastern Europe will be importing less wheat, while the latter will be importing more feed grains, from the free world by 1970, assuming average weather conditions between now and then. The size of these markets in any one year is expected to depend on (a) a basic market in the USSR for 1 - 2 million tons of wheat, largely to enable it to meet its domestic requirements in the Soviet Far East and its commitments to Cuba; and (b) an

* The USSR has contracted to buy 3 million tons from Canada and 1 million tons from France. Poland is considered likely to buy 1 million tons, and Yugoslavia 600,000 tons. Since the U.S. Government shipping restrictions do not apply to these last two countries, it is probable that some portion of their purchases will be from the U.S. Romania, which is also not affected by the U.S. shipping restrictions, is not likely to buy any wheat from the free world. Of the East European countries affected by the shipping restrictions, Albania is not considered likely to buy any wheat from the free world; Bulgaria is expected to buy nearly 200,000 tons, of which 100,000 tons is already committed to come from Canada; Czechoslovakia may need 5 - 600,000 tons, of which 300,000 tons are already committed from Canada and France; East Germany may need 5 - 600,000 tons, of which Canada is already committed to supply 318,000 tons; and Hungary might buy as much as 100,000 tons, of which 50,000 tons is reported coming from Canada. In addition, it is estimated that Australia and Argentina, which harvested their wheat last December, may sell some to North Korea and various countries of Eastern Europe, respectively.

CONFIDENTIAL

-5-

unpredictable Soviet demand for additional wheat because of domestic crop failures; and (c) an apparently stagnating market for wheat in the restricted East European countries (as well as in Poland, Romania and Yugoslavia), coupled with a growing demand in Czechoslovakia, East Germany, Hungary and Bulgaria (as well as Poland) for free world feed grains. The main elements of uncertainty involve the future level of Soviet wheat production.

Wheat and the USSR

In the judgment of agricultural experts in CIA, Agriculture and State, Soviet leaders have adopted more rational plans for agriculture, particularly wheat production, and they are taking more concrete steps, as well as exhibiting more determination to implement these steps, than had been the case heretofore. If these programs are carried out at presently estimated rates of plan fulfillment, given average weather conditions, the Soviet Union would regain its position as a net wheat exporter by 1970/71.*

* On December 27, 1966, Agriculture Minister Matskevich announced that the 1966 Soviet grain crop would be a record 171 million tons, but no official estimate for wheat is available. The official grain estimates are, however, known to be inflated. The actually usable crop of wheat in 1966 is estimated by U.S. specialists on Soviet agriculture at roughly 70 - 75 million grain tons; that of all grains at 135 million tons. This compares with 48 million tons of wheat and 100 million tons of all grains, respectively, harvested in the poor crop year of 1965. No quantitative estimate of the USSR's grain "surplus" is available. We believe, however, that it can be described as "substantial". Most of the surplus is likely to be stored as a hedge against a future poor crop year, since replenishing depleted government grain reserves has a high priority.

CONFIDENTIAL

CONFIDENTIAL

-6-

On the other hand, Soviet performance in realizing previous programs for boosting agricultural output has been poor, and substantial achievement of the plans now being implemented would be a radical departure from experience. Partially due to adverse weather in four of the past five years, grain production has tended to stagnate. In each of the crop years 1963/64 and 1965/66 the Soviet Union purchased about 10 million tons of wheat from free world sources to meet domestic needs and export commitments.

A careful analysis of recent Soviet measures to enhance production indicates the likelihood of progress in the achievement of planned goals. However, in the event of major shortfalls in inputs, a weakening of incentives and mediocre weather, growth might lag sufficiently to require a rising average level of Soviet purchases from the free world. Soviet import needs might then be substantial in the event of crop failures of the magnitudes experienced in 1963/64 or 1965/66. Moreover, a Soviet internal demand for grains as animal feed may be a growing factor in the behavior of this market. Whatever Soviet needs may be, the over-all state of U.S.-Soviet relations will be a basic determinant in any Soviet decision to purchase wheat from the United States. They would have to be faced with a pressing need with no other reasonable alternatives before they would buy U.S. wheat, unless the Vietnam conflict is resolved.

CONFIDENTIAL

-7-

The most probable outlook is for a substantial and relatively successful Soviet effort to achieve an increase in grains output, but the impact of this effort is expected to become more apparent as 1970/71 approaches. Soviet planners appear to have hedged in this direction by contracting with Canada for average imports of 3 million tons yearly through 1968/69.

Feed Grains and Eastern Europe

Demand by the restricted and non-restricted countries of Eastern Europe for free world feed grains was not significant until 3-4 years ago, when it began to grow because of increased demand there for meat, poultry and dairy products. The USSR grows large amounts of corn and other feed grains, supplies quantities to Eastern Europe, and is not likely to need any from the free world in the foreseeable future. The East European countries that will most probably import substantial amounts of feed grains between now and 1970/71 are, among the restricted countries, Czechoslovakia, East Germany, Hungary and Bulgaria. Of the non-restricted countries, Poland will probably continue to import feed grains from the free world, while Yugoslavia and Romania are more likely to be exporters than importers, except in years of poor harvests.

U.S. and Other Free World Suppliers of wheat and Feed Grains

Wheat. In recent years, Canada, Australia, France and Argentina have been supplying most of the wheat imported by the Communist countries of Europe and Asia. By 1970/71 they are likely to have a combined exportable surplus of 13-14 million tons, after supplying their domestic and free world customers. They could further increase their production if Communist demand should be heavy. On that basis, they could meet any likely Communist

~~CONFIDENTIAL~~

-8-

world deficit between now and 1970/71, unless unusual production difficulties should raise it substantially above the foreseeable figure of 12-14 million tons per annum. Between 6 and 8 million tons of this amount are expected to be purchased by Communist China.

Putting aside political problems in our relations with the USSR and Eastern Europe, the consequence of these free world availabilities is that the USSR and the East European countries are not likely to seek U.S. wheat, unless it can be bought at a price and under conditions (e.g., credits) which are entirely competitive with those of other free world producers.

At present, U.S. firms cannot compete for this business because of the cargo preference rule. This rule, if applied strictly on a 50-50 basis, would raise the average price of U.S. wheat delivered to a Black Sea port by \$4.50 - \$6.00 per ton. That added cost factor is enough to preclude most Communist countries from buying any wheat from us, except in years of crop disaster, as in 1963/64.

If the 50-50 shipping rule were abandoned, U.S. firms could expect to share with other free world countries in supplying the USSR and Eastern European markets for wheat, whenever they would exist. How much of such business we could expect to get would depend, among other things, on US-USSR relations, and in particular, the severity of Soviet differences with us over Vietnam.

~~CONFIDENTIAL~~

~~CONFIDENTIAL~~

-9-

The amount of such potential U.S. sales of wheat, if we abandoned the 50-50 shipping rule with respect to the USSR and the restricted countries of Eastern Europe, is, of course, uncertain. Our only wheat sale since 1964, in which the 50-50 shipping requirement was applied, was for 40,000 tons sold to East Germany, notwithstanding the restrictions.* Maritime nations complained about this transaction as a treaty violation. At the selling price of U.S. wheat, FOB Gulf Port, we could expect to gain around \$65 million for each million tons of wheat we might be able to sell to the USSR and Eastern Europe.

Feed Grains. The U.S. presently supplies approximately 50% of world demand. Other free world producers are numerous, have comparatively small surpluses, and generally little margin for substantially increased production. We have sufficient land in reserve to grow as much as 45 million tons more by 1970.

The U.S. already sells feed grains in the East European market. Access to a portion of this market is impeded, however, by the application of the 50-50 shipping rule and its part-cargo exception. As stated above, the part-cargo rule operates to waive the 50-50 rule, and allow shipment entirely on foreign flag vessels, if part of each cargo for one of the restricted countries of Bulgaria, Czechoslovakia, Hungary, East Germany and Albania is destined for a free world country and is off-loaded at a free world port, including Yugoslavia, but excluding Poland and Romania. Full cargo shipments may, however, go on foreign flag vessels directly to

* In 1964 we sold Poland, a non-restricted East European country, about 700,000 tons of wheat, for \$47 million. In 1965, Poland bought from us about 9,000 tons for about \$560,000, while in 1966 we sold her about 200,000 tons, for about \$13 million.

~~CONFIDENTIAL~~

CONFIDENTIAL

-10-

Poland, Romania and Yugoslavia, as they are not affected by the 50-50 rule or the part-cargo exception, except that Polish and Romanian ports are not treated as free world ports for part-cargo unloading purposes. This need to off-load part cargoes at West European or Mediterranean ports may block some sales to some of the restricted East European countries because of the inconvenience of arranging such sales. As much as \$1 - \$2 per ton might be added to the ocean freight charges on feed grains delivered to some of the restricted East European countries, if vessels have to discharge part of the cargo at a port in a free world country and the balance at a port in the restricted country.

How much more feed grains the U.S. could sell the restricted East European countries, if the 50-50 shipping rule and its part cargo exception were abandoned,* is difficult to estimate. Indeed, the entire amount those countries may need from the free world annually between now and 1970 is uncertain. It depends on the speed at which they permit the meat, poultry and dairy product consumption of their peoples to rise, their own feed grain production, and their imports from each other and from the USSR.

Government experts estimate that the restricted East European countries are likely to need a total of about 0.75 to 1.25 million tons of feed grains from the free world (over their domestic production and intra-bloc trade) in each of the next few years, and that this amount can grow

* For the reason given above, removal of the so-called "part-cargo rule" alone would not be beneficial.

CONFIDENTIAL

-11-

to as much as 1.75 million tons a year by 1970/71. USDA experts believe that, of these amounts, U.S. firms should be able to sell the restricted countries about 2/3, or between 500,000 and 840,000 tons, of their free world purchases, in each of the next few years, and 1.15 million tons a year by 1970/71.

The foregoing estimates cannot, of course, be considered attainable only by repeal of the 50-50 rule and the part-cargo exception. In 1965/66, with the part-cargo exception to the 50-50 rule in effect, U.S. firms managed to sell an aggregate of nearly 1 million tons of feed grains to the restricted Eastern European countries. The bulk of those U.S. sales went to East Germany and Czechoslovakia, which may have paid an extra charge for receiving the grains through Hamburg because of our part-cargo rule.* Hungary and Bulgaria bought smaller amounts from us**--possibly because our part-cargo rule may have resulted in their having to pay an added charge for unloading part of each cargo at a port in the free world, or possibly because of lack of funds, or for other reasons.

* Between January 1, 1965 and June 30, 1966, the U.S. exported to Czechoslovakia \$2.5 million of barley, \$11.7 million of corn, \$18 million of grain sorghums, and \$5.5 million of soybeans, which is used for feed, but not considered by us as a feed grain and therefore not subject to the 50-50 and part-cargo rules. In the same period, we exported to East Germany \$11.8 million of corn, \$3.1 million of grain sorghums, and \$560,000 of soybeans.

** Between January 1, 1965 and June 30, 1966, we exported to Bulgaria \$2.2 million of soybeans. In the same period, Hungary imported from us \$286,000 of corn, \$954,000 of grain sorghums, and \$7.1 million of soybeans.

CONFIDENTIAL

-12-

Agriculture experts suggest, however, that our 1965/66 experience was abnormal, as the West European countries which normally compete with us in selling feed grains to the restricted countries of Eastern Europe, as well as several of the East European countries themselves, had poor harvests that year. They also estimate that in 1966/67 the production of the restricted countries will be up, so that their aggregate imports from the entire free world in 1966/67 will probably be below 1 million tons. On that basis they suggest that our potential sales of feed grains to these restricted countries would have been only about 400,000 - 500,000 tons, even if we had removed the 50-50 rule and the part-cargo exception at the beginning of this crop year. On the other hand, they estimate that our 1966/67 sales to these countries will be at least 300,000 tons, even though we retain our shipping restraints to the end of this crop year.

Our financial benefit from any increased sales of feed grains to the restricted countries of Eastern Europe can be estimated on the basis of the selling price of U.S. yellow corn, which is currently about \$60 per ton, FOB, New Orleans. On this basis, each additional 1,000 tons we might be able to sell them by dropping our shipping restriction would add \$60,000 to our exports and thus to our balance of payments position.

There is currently being considered within the Executive Branch a proposal that a U.S. mission be formed to go to various Eastern European countries to seek added markets there for U.S. feed grains. At this time, however, no determination has been made as to the precise nature of the proposed mission, its membership, and when and where it would go.

CONFIDENTIAL

-13-

Nature and Background of U.S. Government Restraints

Exports of wheat and feed grains are not embargoed to the USSR and Eastern Europe. Validated licenses are required by Commerce for such exports, under the Export Control Act. As previously stated, the purpose of requiring licenses for such peaceful goods is basically to enable Commerce to see that U.S. Government shipping restraints on such trade are observed. The Commerce requirement for such licenses is, of course, a government-imposed restraint, but it is not considered much of a burden to sellers or obstacle, by itself, to our trade. However, it seems clear that if the shipping restraints were abolished, all agencies concerned would agree to placing these products under general license to all of Eastern Europe.

Cargo Preference Rule

The chief obstacle to our selling any wheat or feed grains to the USSR, and wheat to the restricted East European Communist countries is, as indicated, our special requirement that 50% of such grains to those countries must be carried in U.S.-flag ships.* Freight rates for U.S.-flag ships to the USSR are currently \$9 to \$12 a ton higher than rates charged by foreign flag vessels. This amounts to a 7.5% increase in the export price of U.S. wheat and an 8.5% increase in the export price of

* Shipping restrictions applicable to feed grains are described on pages 9-10. Shipping restrictions applicable to wheat are as follows: The 50-50 rule applies to the USSR, Czechoslovakia, Hungary, Bulgaria, East Germany and Albania, with no provision for a part-cargo exception.

CONFIDENTIAL

~~CONFIDENTIAL~~

-14-

U.S. corn. With those premiums to pay, the USSR is not likely to buy any grains and the other restricted countries are not likely to buy any wheat, from U.S. firms, except in cases of dire need and non-availability from other suppliers, e.g., a crop failure in the USSR coinciding with poor stock positions or shipping bottlenecks elsewhere.

Our present 50-50 shipping requirement stems from the decision of President Kennedy, at the time he authorized our sales of wheat to the USSR in October 1963, that the wheat should be carried in "available American ships, supplemented by the vessels of other countries." The American Maritime Association, an association of American Flag ship-owners, had urged President Kennedy to treat such sales as if they were government-to-government transactions covered by the Cargo Preference Law (PL 664). The President rejected that approach, but chose to reach a somewhat similar result under the Export Control Act, which authorized the President to control exports and to issue licenses subject to conditions.

When it was early found that U.S.-flag ships would probably not be available in sufficient numbers and times to move more than half the expected Soviet purchase, the decision was made that "at least 50% U.S.-flag participation" would be the goal.

The International Longshoremen's Association then announced its willingness to handle the shipments on the 50% basis. This was a breach in that Union's stated policy, which is infrequently applied, of refusing

~~CONFIDENTIAL~~

~~CONFIDENTIAL~~

-15-

to handle some Communist country freight. The Union, from then on, sought to maintain the requirement. It strongly opposed Maritime Administration grants of waivers in 1963/64, which allowed more than 50% of some shipments to Hungary and the USSR to go in foreign-flag ships.

The resulting controversy with the Unions led to revision of the Commerce Department's export regulations to make it clear that the 50-50 shipping rule applied to both wheat and feed grain purchases by the USSR, and to wheat and wheat flour shipments to Eastern European countries, other than Poland, Romania and Yugoslavia.* In effect, exceptions to the 50-50 requirement for wheat shipments were to be disallowed. It appears, although we are unable to document this, that it was also decided at high level that Commerce should extend the 50% shipping rule, without publication, to feed grain shipments to the East European countries, other than Poland, Romania and Yugoslavia. As previously noted, the requirement was not applied to the latter three countries because both wheat and feed grain could go to them under Commerce Department general license in accord with the U.S. policy to treat them more liberally than other Communist countries. It is understood that the Unions and the ship owners knew of and accepted those procedures.

By late 1964, it was decided that it would not be commercially feasible to apply the 50-50 requirement to a single cargo (10,000 tons) of feed grain to a restricted East European country. The exporter in the particular

* Publication of the restriction for wheat shipments was in Commerce Current Export Bulletin No. 890 (March 11, 1964).

~~CONFIDENTIAL~~

CONFIDENTIAL

-16-

case was allowed to ship it in a 10,000 ton foreign-flag ship, but was cautioned by Commerce that any subsequent licenses would be subjected to the 50-50 rule, calculated retroactively to include this first shipment.

Part-Cargo Exception

The genesis of the part-cargo exception to the 50-50 rule is, as follows: In late 1964, an exporter applied for a license to ship 23,000 tons of corn to East Germany as part-cargo on a large (30,000 ton) foreign-flag vessel, along with 7,000 tons of other goods which were to be unloaded at a West European port. Although this shipping arrangement was approved in principle, no license was issued in the particular case because the transaction fell through. Other exporters, however, later applied for and were allowed licenses on a similar basis. In theory, the foreign-flag ship could first unload the other cargo in the West European port or Mediterranean and then proceed to a port in a restricted East European country to unload the balance of the cargo. This proved not generally commercially feasible. Most cases in which such licenses were issued have therefore involved unloading the full cargo in the free world port, with inland or other transshipment of the portion licensed to the restricted East European country by other means of transportation. No published regulation deals with this procedure.

Since each such license application is in effect treated as a separate transaction, this so-called part-cargo unloading practice, is essentially a relaxation of the unpublished 50-50 rule. As previously stated, doing away with the part-cargo rule above would put exporters back in the situation of having to ship under the unpublished 50-50 rule, unless that rule too were dropped.

CONFIDENTIAL

CONFIDENTIAL

-17-

A modest improvement could be made in operation of the part-cargo rule by treating Poland and Romania (in addition to Yugoslavia) as if they were "free world" destinations for the purpose of destining and unloading the first part of a cargo in their ports and for allowing the onforwarding of the "balance" from their ports to restricted countries like Czechoslovakia, East Germany, Hungary and Bulgaria. Over-all, however, the real issue is still the 50-50 cargo preference rule and the potential labor union and ship owner reaction to relaxing or doing away with it.

As stated, the officials of the several departments and agencies who took part in this study have not been able to ascertain clearly:

1. Whether the unpublished 50-50 shipping requirement on shipments of feed grains to certain countries of Eastern Europe, other than the USSR, was imposed as part of the Administration's effort to induce the Longshoremen's Union to load the grain ships.

2. Whether the unpublished part-cargo unloading exception to the unpublished 50-50 shipping requirement on feed grains to certain East European countries was specifically made known to and accepted by the labor unions concerned.

CONFIDENTIAL

~~CONFIDENTIAL~~

-18-

CONCLUSIONS

The issue raised in this study is whether economic and foreign policy benefits considered likely to result from removal of these U.S. restrictions on wheat and feed grain sales to the USSR and certain East European countries outweigh possible detriments that might result from political, labor and ship owner objections to such action, including labor reprisals and the difficulty of doing anything effectively about them. The main conclusions are as follows:

1. USSR and EE have become an important market for wheat and to a lesser extent coarse grains. In this crop year (ending June 1967), the USSR will probably buy about 4 million tons of free world wheat pursuant to commitments already made with Canada and France. The restricted and unrestricted countries of Eastern Europe are expected to purchase approximately 2.5 million tons of wheat from the free world, i.e., Canada and France, plus some from the U.S. to the unrestricted country of Poland. In an average crop year between now and 1969/70, it is unlikely that the USSR will seek additional wheat from the free world beyond the 3 million tons a year already contracted for from Canada. By 1970, under average conditions, the Soviets may be in the market for about 1-2 million tons. If, however, the USSR were to experience a bad crop, its purchases would probably be greater.

With respect to all of the East European countries the demand for free world wheat in an average crop year is estimated to be in the order of 2-3 million tons between now and 1970, of which the restricted countries would take about 1-2 million tons, mainly from Canada and France. In a bad crop year, this could rise to about 3 million tons to the restricted

~~CONFIDENTIAL~~

CONFIDENTIAL

-19-

countries, though their dependence on the free world would be affected by the availability of supplies from the USSR. Feed grain imports by the restricted countries of Eastern Europe are likely to be about 0.75 million tons this crop year. Their demand for feed grains will be increasing through 1970 and, if 1970 is a year of average weather, those countries might import as much as 1.75 million tons. If it is a bad crop year, they might import more.

2. Competition for Communist wheat markets will be keen because free world commercial demand (as distinct from food aid) is stagnating. At the same time, wheat production is being expanded in the U.S., Canada, Australia, Argentina, France and the U.K. This increased production will be pressing on commercial markets, even if allowance is made for their and our increased food aid programs.

3. The long-run U.S. economic advantage lies in our becoming competitive in Communist country markets for grains. The U.S. now accounts for a quarter of wheat sales to free world commercial markets, but we make only occasional sales to the restricted East European Communist countries and the USSR. Under freely competitive conditions the U.S. can, in time, gain a share in those markets commensurate with its position in other markets. The U.S. could expect to supply possibly two-thirds of the coarse grain import needs of the restricted East European countries, in view of its dominant position as supplier of such grains.

CONFIDENTIAL

4. Full U.S. participation in grain exports to the restricted East European Communist countries depends on the removal of the shipping impediments which make our grains non-competitive. The 50-50 shipping requirement adds 7-9% to the delivered cost of U.S. grains in the USSR and in the restricted countries of Eastern Europe. The prohibition of full shiploads in foreign-flag vessels can possibly add as much as 2-4% to the delivered cost of U.S. feed grains to some of the restricted countries of Eastern Europe. This part-cargo requirement benefits only competing foreign suppliers. Since the extra cost resulting from the part-cargo exception (when it occurs) is only about \$1-\$2 per ton, compared with a differential of between \$9 and \$12 per ton when U.S.-flag ships are used, it can be assumed that all present shipments of U.S. feed grains to the restricted countries of Eastern Europe move in foreign-flag ships.

5. Removal of the 50-50 shipping requirement would not increase U.S. wheat exports to the USSR this crop year. Soviet wheat production is larger than it has been in any recent year. Moreover, the USSR has a contractual arrangement with Canada for 3 million tons each year through 1968/69, and with France for an additional 1 million tons in this crop year.

6. The U.S. could make additional feed grain sales in the future to the restricted countries of Eastern Europe, if we were free of the unpublished 50-50 shipping preference and part-cargo unloading exception. With these restrictions, we probably will sell this year between 250 and 300 thousand tons of feed grains to the restricted countries of Eastern Europe. Without them, we may, by 1970, be able to double, or even more than double, that volume to those countries; while with the restrictions there would probably still be some growth, it is believed that the amount would be significantly less. Indeed, it is believed

CONFIDENTIAL

-21-

that without the restrictions some additional amount might still be sold to one or more of these countries before the end of this crop year (June 30, 1967).

7. The U.S. balance of payments could gain in the long run from removal of these special shipping requirements. This could be on the order of \$100 million annually from wheat sales and as much as \$50 million a year from feed grains, by 1970/71, assuming average crop conditions. However, in the absence of a Vietnam settlement, we believe the Soviets would have to be faced with a pressing need, with no other alternatives, before they would buy U.S. wheat. Other factors, such as ability to pay, will also affect the level of purchases by the East European restricted countries.

8. Our ability to maintain a flexible and forthcoming posture in East-West trade is impaired by existing U.S. impediments to trade in grains. Removal of these impediments would constitute an important new initiative which would further the President's objective of encouraging our trade with the USSR and other Eastern European countries in non-strategic goods.

9. The removal of the 50-50 shipping requirement for commercial grain shipments would remove a standing inconsistency with our treaty obligations to various friendly countries not to discriminate against their vessels in foreign commercial trade. Treaties of Friendship, Commerce and Navigation with 30 countries prohibit such discrimination.

10. The major thrust of the President's policy toward the USSR in the economic area involves the removal of the various restrictions which have served to reduce trade to a minimum. In this case, a restriction which serves no real purpose and is a source of annoyance to the Soviets can be removed without legislative action.

CONFIDENTIAL

CONFIDENTIAL

-22-

11. The main obstacle to a removal of these shipping requirements is the previously expressed or anticipated opposition of the maritime unions. This is true, even though these requirements, while damaging U.S. economic and political interests, have demonstrably failed to benefit U.S. shipping. Opposition centers in the National Maritime Union, the Seafarer's International Union and, most important, the International Longshoremen's Association, which is in a position to make its views felt by refusing to load. The maritime unions have been supported by the AFL-CIO. The participants in this study, nevertheless, agree that no repeal or removal of the 50-50 rule as to wheat for the USSR or for the affected countries of Eastern Europe should be undertaken without prior consultation with labor leaders, to the extent such consultations are warranted by commitments to labor. The same is true of the unpublished application to feed grains of the 50-50 rule and the part-cargo exception for certain countries of Eastern Europe.

12. There are risks in raising the subject with labor at this time. If Labor is strongly opposed to rescinding these rules, the risks might include (a) a boycott on foreign shipping, particularly the vessels of countries in East-West Trade; (b) shipping tieups which could interfere with cargo for Vietnam; (c) labor pressure for extension of 50-50 to all cargo for the USSR and Eastern Europe, i.e. making shipments now subject to the part-cargo rule fully subject to 50-50, or extending the present

CONFIDENTIAL

CONFIDENTIAL

-23-

coverage of 50-50 to all countries in Eastern Europe and all cargo to that region; (d) heightened labor opposition to further U.S. East-West trade initiatives; and (e) labor insistence on a larger government assistance to the U.S. maritime industry to offset the real or imagined injuries of rescinding present restrictions. Although U.S. flag shipping is fully employed now and for the foreseeable future in the Vietnam sea lift and the carriage of Agriculture and AID cargoes, there are still risks in raising this issue with labor at this time.

13. Uncertain Nature of Commitment to Labor. The basis for applying the 50-50 shipping requirement, and the part-cargo exception, to feed grains, is not a matter of record in any of the agencies participating in this study. Therefore, the exact nature of any commitment to labor on these unpublished rules is uncertain. However, government officials in the several agencies (Labor, Maritime Administration and State) which deal with the maritime labor unions are of the opinion that the operation of the various restrictions, both written and unwritten, is known to the labor unions.

14. Discussions with labor might better be addressed to the cooperation of maritime unions with government programs to improve East-West trade relations. Putting the narrow question of rescinding these or some part of these regulations to labor invites a confrontation, whereas, in a broader context, this issue becomes only one element in seeking the major foreign policy objective of improved East-West relations.

CONFIDENTIAL

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RECOMMENDATIONS TO THE PRESIDENT

1. The 50-50 shipping rule and part-cargo exception only interfere with possible sales to Communist countries that would benefit our agricultural sector and our balance-of-payments, and they are of no benefit to American labor.

2. There probably would be political costs in eliminating the 50-50 requirement as related to the Soviet Union because of the "dug-in" labor position on handling cargo for the USSR. Eliminating the part-cargo exception alone would not be helpful as it would leave the more restrictive 50-50 rule in effect.

3. It would be desirable to have both the 50-50 and part-cargo requirements eliminated. With respect to wheat, there would be no special advantages in seeking elimination of the restriction this year as no large sales are in prospect. However, getting rid of the 50-50 rule and the part-cargo exception on feed grains to the restricted countries of Eastern Europe (Albania, Bulgaria, Czechoslovakia, East Germany and Hungary) might permit some increased sales even now. Indeed, in connection with the proposed U.S. mission seeking markets for feed grains in various East European countries, it is important that we be prepared to remove restrictions on shipments of feed grains. We doubt that such a mission could be expected significantly to expand U.S. feed grain sales to the restricted countries, if the restrictions are maintained.

CONFIDENTIAL

CONFIDENTIAL

-3-

C. Seek the much more limited objective of allowing part-cargoes of feed grains to be unloaded in the unrestricted countries of Poland and Rumania, just as they presently may be unloaded in West European and Mediterranean ports, including Yugoslavia. This could reduce the unloading cost and thus facilitate increased sales of feed grains to Hungary and Bulgaria, and possibly also to East Germany and Czechoslovakia.

APPROVE: _____

DISAPPROVE: _____

D. Make no change in the existing rules at the present time.

APPROVE : _____

DISAPPROVE : _____

CONFIDENTIAL

The Honorable Alexander B. Rowbridge
The Acting Secretary of Commerce
Department of Commerce
Washington, D. C. 20230

Dear Mr. Secretary:

In response to your request we have examined the summary and conclusions of the interagency study dated 1 March 1967 dealing with prospects for US exports of grain to European Communist countries through 1970.

CIA's contribution to this paper was limited to the demand and supply position of Communist countries and the current commitments of free world nations to provide grain to these countries in the future. Much of this material has been incorporated in the interagency paper and we have no problems with the treatment of these topics. In addition to an analysis of the market situation, the paper as you know contains recommendations to the President and offers him four alternative courses of action. It is, of course, not appropriate for me to comment on policy matters of this kind.

Sincerely,

Richard Helms
Director

Concur:

(31)
EDWARD W. PROCTOR
Acting Deputy Director for Intelligence

17 March 67
Date

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